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In the Supreme Court of the United States

OCTOBER TERM, 1961

No. 575

AMERICAN SURETY COMPANY OF NEW YORK, PETITIONER

v.

SUNDBERG & SONS, ET AL., AND THE UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF WASHINGTON

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The memorandum decision of the Superior Court of King County, Washington, is not reported. The opinion of the State of Washington Supreme Court (Pet. 1a–15a) is reported at 363 P. 2d 99.

JURISDICTION

The petition for rehearing of the decision below was denied on August 29, 1961, and judgment was entered by the Supreme Court of Washington on August 31, 1961. The petition for a writ of certiorari was filed on November 27, 1961. The jurisdiction of this Court is invoked pursuant to the 28 U.S.C. 1257.

QUESTION PRESENTED

Whether federal tax liens take priority over a mortgage purporting to secure future advances, when the advances were not made until after notice of the tax liens was filed.

STATUTES INVOLVED

The statutes involved, Sections 6303, 6321, and 6323 (a) and (b) of the Internal Revenue Code of 1954, are set forth in the Appendix, *infra*, pp. 10–11.

STATEMENT

In February, 1955, Oscar Sundberg, Thor Sundberg, and Carl Sundberg, doing business as Oscar Sundberg and Sons, a partnership, entered into a contract with the Boeing Airplane Company to do certain painting for the sum of $341,569. The Sundbergs, as principals, entered into a performance bond with the American Surety Company providing that, if the Sundbergs were unable to perform the contract, the surety was required to complete it. (Pet. 1a.)

On July 14, 1955, the Sundbergs were unable to continue performance of the contract because they did not have sufficient funds to meet labor expenses. At their request, the surety advanced $9,000 to them; it was agreed that this sum would be secured by a mortgage. On July 19, 1955, the Sundbergs obtained another advance of $3,077. That day Thor Sundberg, on behalf of himself and the other partners, assigned to the surety all of their claims against Boeing; the Sundbergs also executed mortgages in

favor of the surety on real property which each individually owned. Three of the mortgages were recorded in King County, Washington, on July 20, 1955, and the fourth in Island County on July 21, 1955. The mortgages, which were practically identical except for the mortgagor's name and the property described, stated that they were in consideration of the $9,000 advanced July 14th (Pet. 1a–2a, 17a):

> * * * and in further consideration of the advance at this time of Three Thousand and Seventy-Seven and 74/100 ($3,077.74) Dollars, and in consideration of further advances to be made, and to secure the total sum now advanced amounting to Twelve Thousand and Seventy-Seven and 74/100 ($12,077.74) Dollars, according to the terms of promissory note bearing date of July 19, 1955, * * *.

Additional advances were made until August 9, 1955, for which the Sundbergs gave their joint notes. Subsequent to August 9, 1955, the surety's advances were not made directly to the Sundbergs but were made to materialmen and others; the Sundbergs gave the surety no notes after that date. (Pet. 2a.)

The total amount advanced by the surety to complete the contract was $163,316. The surety received credits and payments on account of the contract in the amount of $106,747. The amount advanced by the surety for which it did not receive reimbursement was therefore $56,569. (Pet. 2a–3a.)

The United States assessed withholding taxes, federal unemployment taxes, and penalties and interest

against Oscar Sundberg and Sons. The taxes were assessed and notices of lien were filed in King County as follows (Pet. 3a, 4a):

Tax	Amount of tax	Assessment date	Date notice of tax lien filed in King County
Withholding [1]	$22,626	8/21/56	10/26/56
Withholding [1]	16,106	11/20/56	1/ 4/56
Withholding [1]	3,045	2/ 5/56	3/21/56
Unemployment [2]	1,380	2/22/56	4/18/56
Unemployment [2]	757	7/15/57	

[1] Withholding taxes are imposed on wages pursuant to Sections 3401–3404 of the Internal Revenue Code of 1954 (26 U.S.C. 3401–3404).

[2] Unemployment taxes are imposed by the Federal Unemployment Tax Act, Sections 3301–3309 of the Internal Revenue Code of 1954 (26 U.S.C. 3301–3309).

Notice of the above tax liens was also filed with the auditor of Island County, Washington, on February 17, 1959. Despite demand by the District Director, the taxes were not paid. (Pet. 3a–4a.)

The surety instituted this action in the Superior Court of King County, Washington, to foreclose on the mortgages given by each of the Sundbergs naming as parties the United States and others who had or claimed an interest in the properties.[1] The trial court, after entering judgment for the surety in the amount of $56,569 against the Sundbergs, made a decree foreclosing the mortgages and ordered that the proceeds of the King County property be applied first in payment of the surety's judgment prior to satisfaction of any of the liens of the United States. Upon the government's appeal, the court

[1] Although the surety's petition in this Court titles the case with the partnership name, the partnership is not now and has never been a party to this action.

below modified this order of priority as to the proceeds of the King County property. The court found that all of the $56,569 remaining unpaid had been advanced in installments on or after December 6, 1955, and after all or part of the federal taxes had been assessed and notices of lien filed.[2] (Pet. 3a–4a.) It held that the liens of the mortgages were subordinate to the tax liens insofar as they secured advances made after notice of the tax lien had been filed and were prior to the tax liens insofar as they secured advances made before filing of the tax liens. (Pet. 9a–13a.)

ARGUMENT

Section 6321 of the 1954 Internal Revenue Code (Appendix, *infra*, p. 10) imposes a lien in favor of the United States on all of the property of a person liable to pay any tax who fails to pay after demand. Section 6323(a) (Appendix, *infra*, p. 10) provides that this lien is not valid against a mortgagee (among others) until notice of the lien has been filed.

The surety argues (Pet. 6–8) that the interests described in Section 6323(a) are entitled to priority over any subsequently filed federal tax lien, whether or not choate when the federal lien attaches. This argument, which was the basis of the dissenting opinion in *United States* v. *Bond*, 279 F. 2d 837, 848 (C.A. 4), certiorari denied, 364 U.S. 895, mis-

[2] An exception is a tax lien for $757, not in controversy. (Pet. 4a, 13a.) No issue is raised here or was below as to the order of priority of the proceeds of the Island County property since all advances by the surety were made prior to the filing of notices of tax lien in that county. (Pet. 4a–5a, 13a.)

construes the purpose and effect of Section 6323. The general rule for priority of liens where a federal tax lien is asserted is that a lien under state law which arises and is choate and perfected prior to the time the federal tax lien arises is also prior in right.[5] Section 6323 does not create for mortgage liens an exception to the general rule that priority in time depends upon the time at which a lien becomes choate. It is designed to give priority to mortgage liens even though they arise at a later date than the federal tax lien if the mortgagee was without notice of the federal lien at the time the mortgage lien became choate. It accomplishes this purpose by making the date of recording the effective date of the federal tax lien as against mortgagees. See *United States* v. *Union Central Life Insurance Co.*, decided December 18, 1961, No. 52, this Term. Thus, a mortgage lien is prior in right to a federal tax lien if, but only if, it is perfected and choate prior to the time that notice of the federal lien is filed pursuant to Section 6323. *United States* v. *Ball Construction Co.*, 355 U.S. 587.

The court below correctly applied well-established principles in holding that the surety's mortgage liens on the King County properties became choate only after the advances secured by the mortgages were

[5] See *United States* v. *Security Tr. & Sav. Bk.*, 340 U.S. 47; *United States* v. *New Britain*, 347 U.S. 81; *United States* v. *Acri*, 348 U.S. 211; *United States* v. *Liverpool & London Ins. Co.*, 348 U.S. 215; *United States* v. *Scovil*, 348 U.S. 218; *United States* v. *Galotta*, 350 U.S. 808; *United States* v. *White Bear Brewing Co.*, 350 U.S. 1010; *United States* v. *Vorreiter*, 355 U.S. 15; *United States* v. *Ball Construction Co.*, 355 U.S. 587; *United States* v. *Hulley*, 358 U.S. 66.

made since only then was the lien fixed in amount. *United States* v. *Ball Construction Co.*, 355 U.S. 587; *United States* v. *Security Tr. & Sav. Bk.*, 340 U.S. 47.* No doctrine of "relation back" may be recognized. *United States* v. *Security Tr. & Sav. Bk., supra; New York* v. *Maclay*, 288 U.S. 290. By the time the mortgage lien became choate the federal tax lien had already been made effective against the mortgagee by the filing of the notice required by Section 6323(a). The federal lien was therefore properly accorded priority by the court below.

The decision below accords with the principles enunciated by this Court and further finds direct support in the decisions of those courts which have passed on the question, including one in which certiorari was denied last term. *United States* v. *Bond*, 279 F. 2d 837 (C.A. 4), certiorari den' 364 U.S. 895; *United States* v. *Christensen*, 269 l .4 (C.A. 9); *United States* v. *Ringler*, 166 F. S . .4; *Metropolitan Life Ins. Co.* v. *United* . es, 9 App. Div. 2d 356, 194 N.Y.S. 2d 168. See a so *Hoare* v. *United States*, 294 F. 2d 823 (C.A. 9). Indeed, no conflict with these cases is claimed.

The surety's argument (Pet. 8–9) that the mortgages amounted to transfers of the Sundbergs' properties, leaving them with no interest to which the government's liens could attach, citing *Aquilino* v. *United States*, 363 U.S. 509, and *United States* v. *Durham Lumber Co.*, 363 U.S. 522, is plainly without

* This Court has stated that a competing lien is choate and perfected when the identity of the lienor, the property subject to the lien, and the amount of the lien are all established. *United States* v. *New Britain*, 347 U.S. 81, 84; *Illinois* v. *Campbell*, 329 U.S. 362, 375.

merit. Certainly, it is settled Washington law that a mortgage is merely a lien for the payment of money and that the real property subject to the mortgage remains the property of the mortgagor. *Bloomer* v. *S. W. Wash. Prod. Cr. Assn.*, 36 Wash. 2d 752, 757, 220 P. 2d 324, 327; *Union Machinery & Supply Co.* v. *Darnell*, 89 Wash. 226, 233, 154 Pac. 183, 186; *Jump* v. *North British Etc. Ins. Co.*, 44 Wash. 596, 599, 87 Pac. 928, 929; *Swanson* v. *United States*, 156 F. 2d 442, 448 (C.A. 9), certiorari denied *sub nom. Spokane Portland Cement Co.* v. *Swanson*, 329 U.S. 800.

Similarly, the argument (Pet. 9–11) that the amounts received by the surety as the Sundbergs' assignee (and surety) under the Boeing contract were (Pet. 10) "already its own money" and (Pet. 11) "could not be regarded as free money available for allocation by the Court" is without merit. Although the surety as assignee (and under principles of subrogation) was entitled to the sums due from Boeing under the contract (*Prairie State Bank* v. *United States*, 164 U.S. 227; Restatement, *Security*, Sec. 141) it was manifestly necessary to apply those receipts against the surety's expenditures to determine the amount that the surety was out-of-pocket on the contract, *i.e.*, the amount for which the Sundbergs are liable (and for which their properties stand as security). Contrary to the surety's assertions, there is no question that the court below properly applied the first in time, first in right principle in listing the priority of the various liens here involved (Pet. 12a–13a).

In Point V of its petition (pp. 11–12) the surety raises two separate issues. The first is whether the government "failed to file its notices of lien in accordance with the requirement of the statute [Section 6323(a)]", and the second is "[w]hether notice [of tax due under Sections 6303 and 6321] to a partnership is sufficient to bind the real property of each person who is a member of the partnership." However, on neither question does it demonstrate error below or allege a conflict with other appellate decisions. We submit that the well-reasoned and fully supported discussion of these questions in the opinion below (Pet. 5a–7a) shows that both were correctly decided.[5]

In sum, the decision below is correct, it is supported by the decisions of this Court, and is not in conflict with any other decision.

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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JANUARY 1962.

[5] *F. B. Baugh, Inc.* v. *Little Lake Lumber Co.* (C.A. 9), decided October 18, 1961 (61-2 U.S.T.C., par. 9726) (Pet. 12), deals with the effect on partnership property of a tax lien notice filed in the name of one partner; the case at bar involves the partners' individual properties and notices filed in a partnership name that is descriptive of all the partners

APPENDIX

Internal Revenue Code of 1954 (26 U.S.C., 1958 ed.):

SEC. 6303. NOTICE AND DEMAND FOR TAX.

(a) *General Rule.*—Where it is not otherwise provided by this title, the Secretary or his delegate shall, as soon as practicable, and within 60 days, after the making of an assessment of a tax pursuant to section 6203, give notice to each person liable for the unpaid tax, stating the amount and demanding payment thereof. Such notice shall be left at the dwelling or usual place of business of such person, or shall be sent by mail to such person's last known address.

* * * * *

SEC. 6321. LIEN FOR TAXES.

If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, additional amount, addition to tax, or assessable penalty, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person.

* * * * *

SEC. 6323. VALIDITY AGAINST MORTGAGEES, PLEDGEES, PURCHASERS, AND JUDGMENT CREDITORS.

(a) *Invalidity of Lien Without Notice.*—Except as otherwise provided in subsection (c), the lien imposed by section 6321 shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof

has been filed by the Secretary or his delegate—

(1) *Under state or territorial laws.*—In the office designated by the law of the State or Territory in which the property subject to the lien is situated, whenever the State or Territory has by law designated an office within the State or Territory for the filing of such notice; or

(2) *With clerk of district court.*—In the office of the clerk of the United States district court for the judicial district in which the property subject to the lien is situated, whenever the State or Territory has not by law designated an office within the State or Territory for the filing of such notice; or

* * * * *

(b) *Form of Notice.*—If the notice filed pursuant to subsection (a)(1) is in such form as would be valid if filed with the clerk of the United States district court pursuant to subsection (a)(2), such notice shall be valid notwithstanding any law of the State or Territory regarding the form or content of a notice of lien.

* * * * *

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